

November 16, 1997

MEMORANDUM FOR USAID/Ecuador Director, Thomas L. Geiger

FROM: RIG/A/San Salvador, Wayne J. Watson

SUBJECT: Audit of USAID/Ecuador's Review and Certification
of Unliquidated Obligations for Project and Non-
project Assistance, Audit Report
No. 1-518-98-001-F

This memorandum is our report on the subject audit. In finalizing the report, we considered your comments on the draft audit report and have included them in their entirety as Appendix II.

The report contains two recommendations. Recommendation No. 1 identifies \$568,572 in efficiencies for which a management decision has been made. Action has been taken on \$40,000 of this amount through deobligation. Final action for the remaining \$528,572 will be accomplished when USAID/Ecuador has completed its planned reprogramming of these funds. Please notify the Bureau for Management's Office of Management Planning and Innovation (M/MPI) when the Mission has completed all planned actions on this recommendation. For Recommendation No. 2, final action has been completed through the Mission's revision of procedures related to its review of unliquidated obligations.

I appreciate the cooperation and courtesy extended to my staff during the audit.

Background

Concerned that Federal agencies were recording obligations in situations where no real obligation existed, and that information on which to determine an agency's future funding requirements was not reliable, Congress, with the General Accounting Office and the Office of Management and Budget, developed statutory criteria for determining the validity of an obligation. In order to properly certify the validity and appropriateness of obligated balances, agencies are required to verify their own accounts at least once each year. This verification is commonly referred to at USAID as the Section 1311 review or certification, named after the section of the original authorizing public law.

This audit is part of the Office of the Inspector General's (OIG) worldwide review of USAID's obligations for project and non-project assistance. The OIG's Division of Performance Audits (IG/A/PA) is leading this worldwide effort, with the assistance of auditors from all OIG offices of Regional Inspectors General.

The worldwide audit is limited to obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. It does not cover obligations funded with U.S.-owned local currency, obligations for disaster relief, or obligations maintained by USAID for the Trade and Development Agency.

IG/A/PA randomly selected USAID sites for detailed audit work and also determined the number of unliquidated obligations to be randomly selected and reviewed at each site. A total of 19 sites (USAID/Washington and 18 missions) were selected for review. USAID/Ecuador was among those missions randomly selected for review.

Mission records indicate that, as September 30, 1996, USAID/Ecuador had 229 unliquidated obligations for project and non-project assistance with balances totalling \$17,451,574.

Audit Objective

As part of a worldwide audit, the Office of Regional Inspector General/San Salvador audited selected unliquidated obligations at USAID/Ecuador as of September 30, 1996 to answer the following objective:

Did USAID/Ecuador review and certify its unliquidated obligations for project and non-project assistance in accordance with U.S. laws and regulations and USAID policies and procedures?

Appendix I describes in detail the audit's scope and methodology.

Audit Findings

Did USAID/Ecuador review and certify its unliquidated obligations for project and non-project assistance in accordance with U.S. laws and regulations and agency policies and procedures?

For the items tested, USAID/Ecuador generally followed U.S. laws and regulations and USAID policies and procedures in reviewing and certifying its unliquidated obligations for project and non-project assistance; however, in order to fully comply with USAID procedures, the Mission needed to improve its review process by ensuring (i) proper documentation of its reviews and (ii) adherence to USAID's forward funding guidance.

The audit sample included 15 unliquidated obligations totalling \$720,069. Review of these obligations and their underlying commitments¹ showed that USAID/Ecuador conducted quarterly Section 1311 reviews to ensure that unliquidated obligations and commitments were valid and still needed, making deobligations or decommitments when deemed appropriate. Unliquidated obligations were also properly certified as of September 30, 1996, and valid obligating and commitment documents were executed for all 15 obligations tested. However, as discussed below, the audit identified three sample obligations and seven non-sample obligations with excessive balances totalling \$125,181 and \$495,795, respectively.

Some Obligations Had Excessive Balances

Of the 15 unliquidated obligation sample items reviewed during this audit, three of these obligations as well as seven non-sample obligations had balances as of September 30, 1996 which exceeded anticipated needs, as defined by USAID guidance, by \$125,181 and \$495,795, respectively. At the time of our field work in August 1997, two sample obligations had excessive balances of \$75,857 and four non-sample obligations had excessive balances of \$492,715, totalling \$568,572 which the Mission should take action to deobligate.

¹ GAO's *Principles of Federal Appropriations Law* defines an obligation as "some action that creates a liability or definite commitment on the part of the government to make a disbursement at some later time." USAID Financial Management Bulletin, Part II, No. 14A, defines a commitment as "funds set aside [for an obligation] to pay for the goods or services being procured."

Recommendation No. 1: We recommend that USAID/Ecuador deobligate the \$568,572 in excess obligations as described in Appendix III of this report.

Each year, USAID's Bureau for Policy and Program Coordination issues guidance for the preparation of mission and office budgets. Guidance applicable to the period under audit stated that budgets should be prepared as follows:

New Projects or Activities Obligations should provide funding for at least the first 18 months, but not more than 24 months.

Continuing Activities Obligations should be sufficient to fund anticipated expenses for no more than 12 months beyond the end of the fiscal year in which the obligation takes place.

We reviewed obligation balances as of September 30, 1996, and applied USAID's guidance as follows:

New Activities In general, obligation or commitment balances were considered reasonable if they did not exceed anticipated expenses for a period of 24 months following the date of obligation or commitment, or through September 30, 1997, whichever was later.

Continuing Activities In general, obligation or commitment balances were considered reasonable as of September 30, 1996 if they did not exceed anticipated expenses for the 12-month period ending September 30, 1997, the expiration date of the obligating or commitment document, or the project assistance completion date, whichever was earlier. Balances were considered reasonable as of the time of our audit if they did not exceed the anticipated expenses through September 30, 1998. We also took into account balances of earlier or planned obligations which affected the continuing need for part or all of the unliquidated balance being audited. Any questioned amount was discussed with appropriate mission staff.

In several instances, the Mission did not identify funds in the September 1996 Section 1311 review which are considered excessive as of September 30, 1996. These funds were not identified, in part, because the Mission needed to improve aspects of its Section 1311 and other review processes. For example, the Mission did not review uncommitted balances of unliquidated obligations, nor did it properly document key aspects of the review process. (A discussion of these issues follows on page 5 in our Observations on Internal Controls.) In addition, the Mission did not use USAID's forward funding guidance as a criteria in its Section 1311 review. As a result, the Mission had \$568,572 (\$75,857 from sample items and \$492,715 from non-sample items) in unliquidated obligations which were considered excessive as of the time of our audit, thereby tying up these funds which could have been used for other purposes. The details of these instances are discussed below.

As of September 30, 1996, USAID/Ecuador's Child Survival and Health Project (No. 518-0071) had a total of \$885,000 in obligated but uncommitted funds from various fiscal years going back to 1989. As a result of subsequent decommitments, the amount of funds obligated but not committed under the project grew to \$1,008,000 at June 10, 1997. Based on discussions with project officials and review of project documents, we questioned \$636,000 of the \$1,008,000 for being in excess of USAID's forward funding guidance. These funds, which were for activities administered by the Ministry of Public Health (\$529,000) and CARE (\$107,000), were not included in current work plans and, therefore, it was not anticipated that these funds would be spent prior to September 30, 1997. The \$529,000 related to the Ministry of Public Health is questioned as shown by individual obligation amount in lines B through F of Appendix III. Although the amount of \$107,000 to be administered by CARE was excessive as of September 30, 1996, it was not excessive at the time of the audit since the funds cover budgeted expenditures through April 1998 and, therefore, are anticipated to be spent prior to the end of fiscal year 1998.

Mission officials attributed the large balance of obligated but uncommitted funds to slow project implementation by the host government. They explained that they have had difficulties obtaining a work plan from the Ministry of Public Health for the current fiscal year. In addition, they attributed a large portion of the excess balance for the Ministry of Public Health to a contract with an unliquidated balance of \$346,000, which had expired on December 31, 1994, but could not be closed out and the funds recommitted until September 1996. One project official also commented that Congress earmarks funds for child survival and health and that the USAID Bureau responsible for allocating these earmarked

funds may give the Mission more or less than requested in any given year. For example, he stated they received more this year than requested but may not receive any funding next year, making it difficult to turn down funding in one year if future funding is uncertain. He also pointed out that funding is now received later in the fiscal year rather than early in the fiscal year. For these reasons, the project official indicated that it would be difficult for the Mission to request funding in accordance with USAID's forward funding guidance. While noting the Mission's comments, we nevertheless conclude that USAID's forward funding guidance provides a sound basis for effective management of unliquidated obligations, and therefore we are recommending that these amounts be deobligated. Subsequent to the completion of our field work, the Mission made a management decision to reprogram these funds for other activities.

Another obligation had an unliquidated balance as of September 30, 1996 which exceeded the forward funding guidance by \$49,000, funding a personal services contract through June 1998. These funds were not deobligated because the Mission did not consider USAID forward funding guidance in performing its Section 1311 review, and this amount was excessive as of September 30, 1996. However, it was not considered excessive as of the time of the audit because the funds were programmed to be spent prior to September 30, 1998.

The audit also identified \$40,000 in excessive funding for a cooperative agreement which had expired on September 30, 1995. At the time of the September 1996 Section 1311 review, the Mission was awaiting Advices of Charge in order to fully liquidate the obligation. However, we concluded that the Mission had sufficient information as of September 1996 to know that most of the unliquidated funds would not be used and should, therefore, be deobligated. We estimated that \$40,000 would have been a reasonable deobligation as of September 30, 1996 and this amount is also shown as questioned in Appendix III since it remained obligated at the time of our audit. Subsequent to our audit these funds were deobligated by the Mission.

Observations on Internal Controls

While conducting our fieldwork at USAID/Ecuador, we observed that certain USAID and Mission procedures related to the review and certification of obligations for project and non-project assistance were not being followed.

Recommendation No. 2: We recommend that USAID/Ecuador strengthen its procedures and supervision of the Section 1311 review process to ensure (1) proper documentation of the review, (2) inclusion of USAID forward funding guidance as a criterion for the review, (3) inclusion of uncommitted obligation balances in the scope of the review and (4) required notifications of expired contracts, grants, and cooperative agreements.

USAID Financial Management Bulletin, Part II, No. 14A, provides detailed guidance on how missions are to conduct their section 1311 reviews. In addition, USAID's Bureau for Policy and Program Coordination has issued guidance on forward funding of mission activities. USAID/Ecuador also developed local procedures to provide guidance to their staff on how the reviews are to be conducted. However, in several cases, the Mission did not follow agency guidance or their own procedures. In our opinion, improved Mission procedures and supervision of the Section 1311 review process would have prevented these exceptions from occurring, and it is likely that the \$568,572 in excessive unliquidated obligations noted in our audit would have been identified and addressed in the September 1996 Section 1311 review. Discussed below are the details of these management control deficiencies.

USAID guidance states that the Mission accounting reports used in Section 1311 reviews must be annotated to show (1) the date of the review and the names of the reviewers, (2) the decision made with regard to the individual obligation/commitment accounts, including the summarized rationale for the decision, and (3) related actions that should be taken to appropriately adjust the affected accounts. Mission controllers must assure a high standard of documentation and level of analysis that would lead any auditor to conclude that (1) a careful review of each unliquidated obligation and commitment document was conducted, (2) the review was properly documented, and (3) the findings and conclusions are supported by the analyses and documentation. USAID/Ecuador's local operating procedures also incorporate similar notation requirements for each unliquidated obligation/commitment.

The audit showed that the Mission's Section 1311 review working papers did not always contain adequate documentation. Some items lacked the reviewer's name and date on the review sheets, and others had insufficient or no notations regarding the decision made with regard to the individual obligation or commitment accounts. Decision notations were considered insufficient if they did not meet the requirements of USAID guidance, such as including the decision made with regard to the obligation or commitment and the summarized rationale for the decision. Below is a summary of the exceptions noted regarding the 12 sample items² which were included in the Mission's September 1996 Section 1311 review:

Name and date of reviewer on review sheets:	
Sample items without reviewer's name and date	10
Sample items with reviewer's name and date	2
Total	12
Notations regarding 1311 reviewer's decision:	
Sample items with no decision notations	8
Sample items with insufficient notations	4
Total	12

USAID's Bureau for Policy and Program Coordination issues guidance for the preparation of mission and office budgets. This guidance provides that new projects should not be funded beyond 24 months and continuing activities should be funded for no more than 12 months beyond the end of the fiscal year in which the obligation takes place. However, one sample obligation had an unliquidated balance as of September 30, 1996 which exceeded USAID forward funding guidance by \$49,000 because USAID/Ecuador did not consider the guidance in performing its Section 1311 review.

² Of the 15 sample items we reviewed, only 12 were included in the September 1996 Section 1311 review. Two of the other sample items were for funds that were obligated subsequent to the completion of the review, while the third was not reviewed due to the Mission's practice of not subjecting uncommitted funds to review.

USAID guidance and the Mission's standard operating procedures require analyses at both the obligation and commitment levels. However, the Mission's Section 1311 review did not include in its scope a review of uncommitted balances. Therefore, these procedures should be re-emphasized to Mission personnel and, as necessary, supervision should be improved to ensure adherence to these procedures.

USAID guidance requires mission controllers to prepare two separate written communications regarding expired or soon-to-expire contracts, obligations and commitments. First, the controller should report any completed contract, grant, or cooperative agreement to the responsible contracting officer to obtain a decision on the decommitment and/or deobligation of the remaining funds. Second, mission controllers are to periodically prepare a listing of all unliquidated obligations and commitments with expired or soon-to-be expired completion or termination dates. These listings should be provided to mission management for review of the validity of the completion or termination dates. The Mission's standard operating procedures also require written communications to Mission management on a quarterly basis but do not require any communication to the contracting officer. However, according to controller staff, these procedures were not followed. While written communications are sent to Mission management, they identify only projects with expired project assistance completion dates and not individual obligations and commitments that have expired or are soon to expire. Therefore, this requirement should be re-emphasized to the Mission's financial management personnel.

Management Comments and Our Evaluation

USAID/Ecuador generally agreed with the conclusions of our audit report and has begun to take action on the report's recommendations. With respect to the \$568,572 recommended for deobligation in Recommendation No. 1, the Mission made a management decision for the entire amount. It plans to reprogram \$528,572 of these funds for activities to be implemented by the Ministry of Public Health. These activities include \$350,000 under the annual work plan of the Ministry, as well as \$178,572 to be used for controlling an epidemic of snakebites resulting from increased rainfall due to the effect of El Niño. Final action will be achieved when the Mission shows that these funds have been reprogrammed for the activities described above. For the remaining \$40,000, the Mission has already taken action by deobligating those funds, along with an additional \$4,745 related to the obligation. Upon completion of the reprogramming of the \$528,572 described above, a determination of final action will be made by the Bureau for Management's Office of Management Planning and Innovation (M/MPI).

USAID/Ecuador has also implemented procedures to address Recommendation No. 2. The Mission Controller issued guidance prior to the June 1997 and September 1997 Section 1311 reviews, instructing the reviewers to deobligate and decommit funds which are no longer needed and referencing USAID's Financial Management Bulletin on conducting Section 1311 reviews. In addition, the Mission provided recent Section 1311 review sheets which showed that uncommitted balances were included in the review and that the review sheets contained the notations required by the Financial Management Bulletin. The Mission also provided evidence that notifications have been sent to the Regional Contracting Officer and Project Officers listing all expired unliquidated obligations. Finally, with respect to USAID's forward funding guidance, the Mission stated that it has complied with the guidance for continuing activities and will continue to follow the guidance for continuing activities, as well as for new activities. Based on the information provided by the Mission, final action has been completed for Recommendation No. 2.

The full text of management's comments on our report are attached as Appendix II.

Scope and Methodology

This audit is part of the Office of the Inspector General's (OIG) worldwide review of USAID's obligations for project and non-project assistance. The worldwide audit is limited to obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. It does not cover obligations funded with U.S.-owned local currency, obligations for disaster relief, or obligations maintained by USAID for the Trade and Development Agency.

The Regional Inspector General/San Salvador audited USAID/Ecuador's review and certification of unliquidated obligations for project and non-project assistance, as of September 30, 1996. The audit was conducted at USAID/Ecuador, from June 2, 1997 through June 13, 1997, and was performed in accordance with generally accepted government auditing standards.

At the request of IG/A/PA, USAID/Ecuador compiled a list of its obligations for project and non-project assistance which had unliquidated balances on September 30, 1996. The unliquidated balances on this list totalled \$17,451,574. We randomly selected 15 obligations totalling \$720,069 from the list for detailed audit testing. Random sampling will allow the OIG to make USAID-wide projections based on field work performed at a limited number of sites. Because the audit sample as part of the world-wide audit, a materiality threshold was not established for our work at USAID/Ecuador, and our testing was not designed to provide reasonable assurance at the Mission level.

While conducting our fieldwork at USAID/Ecuador, we also performed limited tests of compliance with USAID and Mission procedures related to Section 1311 reviews and pipelines reviews of obligations for project and non-project assistance. Section 1311 review refers to the review of obligations to determine if the requirements of 31 U.S.C., Section 1501(a) (originally enacted as Section 1311 of the Supplemental Appropriation Act of 1955), are met for the validity of the obligations. A pipeline review is defined as a review of obligated, but unliquidated, obligations on the Mission's books.

Because the accuracy and completeness of the mission's list was crucial to our ability to make USAID-wide projections, we interviewed appropriate mission staff about their methodology in preparing the list and reconciled the list and its totals to other mission reports.

Each obligation was reviewed to determine whether it was valid in accordance with the provisions of 31 U.S.C. 1501(a) and decisions of the U.S. General Accounting Office. The results of our field work at USAID/Ecuador will be consolidated with the results of field work conducted at USAID/Washington and other missions and used to make USAID-wide projections.

We also reviewed the unliquidated balance of each selected obligation to determine whether, on September 30, 1996, the balance was needed, in full or in part, to cover anticipated expenses during reasonable future periods. In making these decisions, we considered USAID and Mission guidance for forward funding, activity-specific budgets and spending plans, actual disbursements, progress reports, and accruals. When amounts were questioned, we interviewed relevant activity managers and contracting or grant officers. We also considered prior audits and obtained written representations from Mission management on key assertions related to our audit objective. The results of field work at USAID/Ecuador will be consolidated with the results of field work conducted at USAID/Washington and other missions and used to make USAID-wide projections.

In addition to capturing information and making calculations as of September 30, 1996, for USAID-wide projections, we determined whether the unliquidated balances of any obligations reviewed during the audit still had excess balances at the time of our field work. If so, we recommended that the excess funds be deobligated or decommitted, as appropriate.

United States Agency for
International Development (USAID)
Quito, Ecuador



Agencia de los Estados Unidos para
el Desarrollo Internacional (USAID)
Quito, Ecuador

O/CONT-97-297
October 10, 1997

Mr. Craig Nordby
RIG/A/Sar. Salvador
Unit 3110
APO AA 34023-3110

REF: Draft Audit Report of
Unliquidated Obligations,
No. 1-518-97-00X-P

Dear Mr. Nordby:

We received and thank you for the submission of subject draft report on the Audit of USAID/Ecuador's Review and Certification of Unliquidated Obligations for Project and Non-project Assistance. We have reviewed the report and with regard to the specific recommendations, we have the following comments:

Recommendation No. 1: We recommend that USAID/Ecuador deobligate the \$568,572 in excess balances as described in Appendix III of this report.

- A. On June 23, 1997, we deobligated the amount of \$44,745.89 under CA-518-0094-A-11120 listed as A in Appendix III. Attached are copies of the Cooperative Agreement Amendment No. 6 that was issued to deobligate the funds and the Commitment Liquidation Record report that reflects the transaction of the deobligation.
- B. On the amount of \$528,572.17 listed as B thru F in Appendix III related to project 5180071.00, the Mission requested RIG a reconsideration for not deobligating the funds. We have sent via FAX the following documents that supported our request:
 - 1) FAX dated September 26, 1997, which attached a Memorandum from the Ambassador dated September 24, 1997, urging the Mission to explore the possibility for the utilization of \$178,000.

INTERNATIONAL MAIL ADDRESS: U.S. AID Mission to Ecuador - c/o American Embassy - Quito, Ecuador
U. S. MAIL ADDRESS: USAID, AMEMBASSY QUITO, UNIT 5330 - APO AA 34039 - 3420
FAX NUMBER (593-2) 561-228 PHONE NUMBER (593-2) 232-100

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- 2) FAX dated October 3, 1997, which attached PIL No. 040 dated September 30, 1997, approving the Annual work Plan for the period October 1, 1997, thru September 30, 1998, for which the commitment of \$350,000.00 was recorded. Also attached to this FAX were other documents that justified the purpose and utilization of the balance for \$178,572.17.

The original of the two FAXES mentioned above are attached.

- C. RIG has accepted USAID/Ecuador's proposal, therefore, funds will not be deobligated as recommended under project 5180071.00. See E-mail attached.
- D. For fiscal year 1997, USAID/Ecuador has followed the guidance on forward funding of Continuing Activities for anticipated expenses of not more than 12 months beyond the end of the fiscal year in which the obligation took place. We will continue to follow the guidance, as well as for new Projects or Activities.

Recommendation No. 2: We recommend that USAID/Ecuador review and as appropriate, strengthen its procedures and supervision of the Section 1311 review process to ensure (1) proper documentation of the review, (2) inclusion of uncommitted obligation balances in the scope of the review and (3) required notifications of expired contracts, grants, and cooperative agreements.

- A. Regarding this recommendation and in anticipation of receipt of the draft audit report, on June 27, 1997, the Controller sent a message out to the entire Mission requesting that obligations and commitments be reviewed during the accruals process and to instruct the Controller to de-obligate or de-commit for those items open after the final date of the contract.
- B. As a reminder and follow up to above, on September 25, 1997, the Acting Controller also sent a message to the Mission requesting a careful review especially for projects or contracts that reflected an expired date. In this message, reference was made to FM Bulletin No. 14A which provides detailed guidance on the 1311 Review. All Accountants read FMB No. 14A and the review was made accordingly, with proper notations made on the 1311 Review worksheets; however, Project Managers did not read FMB No. 14A. Deobligations were made where appropriate.

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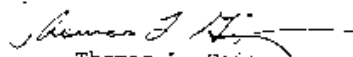
- C. On September 18, 1997, the Acting Controller sent a memorandum to the Regional Contracting Officer and all Project Managers with a report containing obligations and commitments that reflected expired dates. Action was taken before the end of the fiscal year to either extend the dates if required, processed vouchers if received, or deobligate funds where applicable.
- D. During the accruals process, a review was also made on projects that reflected unearmarked/uncommitted funds, with proper notations made on the worksheets.

Copies of the following documents that evidenced actions taken on Recommendation No. 2 are attached: 1) Inter-office E-mail sent to the Mission staff per A. and B. above; 2) Memorandum No. O/CONT-97-266 dated September 18, 1997, sent to the Regional Contracting Officer and all Project Managers with the report mentioned in C.; 3) A sample sheet with notations per D. above.

We are confident that we have taken the actions recommended to strengthen the procedures of the Section 1311 Review process done twice a year.

I want to take this opportunity to thank you and your audit staff for the courtesy and professionalism demonstrated to the Mission staff interviewed during the process of their audit.

Sincerely,


Thomas L. Geiger
Mission Director

cc.

Excessive Obligations as of September 30, 1996
As Determined by Audit

Obligation No.	Excessive Amount	Reason Considered Excessive
CONTR-518-0071-S-01800	\$ 49,176	Excessive Forward Funding
CA-518-0094-A-11120	\$ 40,000	Funds No Longer Needed
PA905180071	\$ 36,005	Funds No Longer Needed
PA895180071	\$ 8,785	Funds No Longer Needed
PA905180071	\$ 34,989	Funds No Longer Needed
PA915180071	\$ 65,510	Funds No Longer Needed
PA925180071	\$ 681	Funds No Longer Needed
PA925180071	\$269,572	Funds No Longer Needed
PA935180071	\$ 43,059	Funds No Longer Needed
PA945180071	\$ 73,199	Funds No Longer Needed
Total	\$620,976	

**Amounts Recommended for Deobligation
As of the Time of the Audit (June 14, 1997)
As Determined by Audit**

	Obligation No.	Amount Recommended for Deobligation	Reason for IG Recommendation
A	CA-518-0094-A-11120	\$ 40,000	Funds No Longer Needed
B	PA905180071	\$ 35,857	Excessive Forward Funding
C	PA895180071	\$ 98	Excessive Forward Funding
D	PA915180071	\$125,758	Excessive Forward Funding
E	PA925180071	\$296,807	Excessive Forward Funding
F	PA945180071	\$ 70,052	Excessive Forward Funding
	TOTAL	\$568,572	